

**LEGISLATIVE SERVICES AGENCY  
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**FISCAL IMPACT STATEMENT**

**LS 6235**

**BILL NUMBER:** SB 288

**NOTE PREPARED:** Jan 1, 2004

**BILL AMENDED:**

**SUBJECT:** Inheritance Tax Exemption for Class A Transferees.

**FIRST AUTHOR:** Sen. Ford

**BILL STATUS:** As Introduced

**FIRST SPONSOR:**

**FUNDS AFFECTED:** ☒ **GENERAL**  
☒ **DEDICATED**  
☐ **FEDERAL**

**IMPACT:** State & Local

**Summary of Legislation:** This bill provides an exemption from the Inheritance Tax for property transferred to lineal descendants and ancestors (Class A transferees) with respect to persons who die after June 30, 2004.

**Effective Date:** July 1, 2004.

**Summary of Net State Impact:** Under the bill, Indiana Inheritance Tax revenues will decrease beginning in FY 2006, but there will be a small compensating increase in Estate Tax revenue in FY 2006. The bill is expected to increase state General Fund expenditures on county Inheritance Tax replacement. The net state impact of the bill is summarized in the table below.

Fiscal Year	Inheritance Tax Revenues	Estate Tax Revenues	State Expenditures for County Replacement	Net Increase (Decrease)
2006	(\$41.2 M)	\$3.6 M	(\$2.4 M)	(\$40.0 M)
2007 and after	(41.2 M)	0.0	(2.4 M)	(43.6 M)

**Explanation of State Expenditures:** The bill could potentially increase expenditures from the state General Fund for county Inheritance Tax replacement by \$2.4 M. Necessary replacement funding may vary depending on whether, and by how much, each county's base revenue differs from the amount guaranteed under current statute. (See *Explanation of Local Revenues*, below, for an explanation of county revenue loss and replacement procedures.)

**Explanation of State Revenues:** The bill is estimated to reduce Inheritance Tax revenue by \$41.2 M beginning in FY 2006. The reduction in Inheritance Tax liabilities is estimated to increase Indiana Estate Tax revenue by \$3.6 M in FY 2006. Estate Tax revenue will decrease to zero in FY 2007 due to the phaseout of the state death tax credit under the federal Estate Tax. Thus, the estimated net revenue loss is \$40.0 M in FY 2006 and \$43.6 M in FY 2007 and subsequent years.

*Background on Inheritance Tax:* Under the bill, transfers to Class A beneficiaries would be exempt from the Inheritance Tax. The change would apply to transfers from persons who die on or after July 1, 2004. Since the Inheritance Tax should be paid within 12 months after the decedent's death (within 9 months to receive the 5 percent early payment discount), the bulk of the impact of the bill would not be experienced until FY 2006. The estimated impact of this change is based on the Revenue Technical Committee's FY 2004 forecast (updated April 10, 2003) and the Office of Fiscal and Management Analysis (OFMA) Inheritance Tax Database. The forecast estimates FY 2004 combined Inheritance and Estate Tax revenues to be \$120 M. Based on a four-year average (2000-2003), 84.6% of the forecast revenue is estimated to be attributable to the Inheritance Tax. From these estimates, the Inheritance Tax will yield about \$101.5 M, and the Estate Tax will yield about \$18.5 M in FY 2004. The estimated share of revenue from Class A transferees is approximately \$41.2 M. This estimate assumes no change in Inheritance Tax revenues through FY 2007.

*Background on Estate Tax:* Although the bill does not make changes to the Indiana Estate Tax, the reduction in Inheritance Tax liabilities for Class A transferees would affect Estate Tax revenues. Under current statute, Indiana Estate Tax is owed on the assets of an estate if (1) federal Estate Tax is owed on the estate and (2) the Indiana portion of the state death tax credit for federal Estate Tax purposes exceeds the total Inheritance Tax paid by transferees of the estate. Under the bill the Indiana Estate Tax would still be limited to estates paying federal Estate Tax, but for some estates the Indiana Estate tax will increase as the Indiana Inheritance Tax decreases. The federal Estate Tax is set to expire in 2005, as will the Indiana Estate tax since it is linked to the federal tax. Therefore, the bill will affect Indiana Estate Tax revenues only for FY 2006.

The estimated impact of the bill on Estate Tax revenues is based on OFMA's Estate Tax database and the Revenue Technical Committee's FY 2004 Estate Tax forecast (updated April 10, 2003) of \$18.5 M. The Estate Tax database consists of 559 estates of decedents who died between July 1, 1997, and June 30, 2000, and that paid Indiana Estate Tax. The exemption of Class A transferees from the Inheritance Tax is estimated to increase the Estate Tax revenues by \$3.6 M in FY 2006.

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:** The bill exempts Class A transferees from the Inheritance Tax. Since the decrease in revenue will likely be larger than the county guarantee payments made by the state, counties will likely experience a net revenue loss of approximately \$1.2 M beginning in FY 2006. The net impact is summarized in the table below.

	Annual Impact Beginning in FY 2006
County Share of Inheritance Tax Revenues (Decrease)	(\$3.6 M)
State Expenditures for County Replacement	\$2.4 M
Net Increase (Decrease)	(1.2 M)

Counties retain 8% of the Inheritance Tax collected on transfers made by Indiana residents. About 99.3% of Inheritance Tax revenue is attributable to the resident Inheritance Tax. Based on the FY 2004 forecast of state Inheritance Tax revenue totaling \$101.5 M, annual county Inheritance Tax revenue will be approximately \$8.8 M beginning in FY 2004. Counties are guaranteed a statutorily determined amount as determined by the replacement provision established by P.L. 254-1997. The replacement provision was established to replace county Inheritance Tax revenue lost when the Class A exemption was increased on July 1, 1997. The replacement provision guarantees that each county receives Inheritance Tax revenue equal to the five-year annual average amount of Inheritance Tax received by that county from FY 1991 to FY 1997 excluding the highest and lowest years. The Inheritance Tax replacement that the state guarantees counties totals \$7.4 M per year.

Currently, most counties retain more in Inheritance Tax revenues than is guaranteed under the replacement procedure and do not receive the guaranteed replacement payment from the state. From FY 2000 to FY 2003, counties exceeded their guarantee amounts by an average of \$4.7 M annually with shortages subject to replacement totaling approximately \$204,886 per year. From the FY 2004 forecast, Inheritance Tax revenues accruing to the counties are expected to total approximately \$8.8 M per year. The Class A exemption would decrease county Inheritance Tax revenues by \$3.6 M. The guaranteed state expenditures for county replacement would offset \$2.4 M of the revenue decrease, and \$1.2 M would not be replaced.

A table showing the amount of Inheritance Tax replacement guaranteed to each county under P.L. 254-1997 is available from the Office of Fiscal and Management Analysis.

**State Agencies Affected:** Department of State Revenue.

**Local Agencies Affected:** Counties.

**Information Sources:** State Revenue Forecast (April 10, 2003), OFMA Inheritance and Estate Tax databases.

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